RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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Nov. 25, 1992 **LETTER 1109**

LOOKING AHEAD: The number one question on investors' minds (aside, of course, from which way the market is headed) seems to be whether president-elect Clinton will be a big spender or a moderate spender. Clinton has been trying to soothe the markets by saying that he's aware of investors' fears, and he has no intention of frightening Wall Street. Clinton is also shrewdly protecting himself by announcing (repeatedly) that the economy is in poor shape (poor shape through no fault of Bill Clinton's).

Clinton is also of the opinion that the economy has to be fired up a bit before he can turn his attention to the deficit. In anticipation of that firing up, the bond market has backed off and short rates have been pushing higher.

As to the economy, I defer to *Industry Forecast* by the Levys from Chappaqua, NY (I've followed them for years, and they have an excellent record on calling the economy). In their latest report they say, *"Poor economic conditions in the major industrial countries are reducing the worldwide demand for goods. Consequently, American exports are now declining, and so are industrial production and manufacturing employment. The profit margins, which increased somewhat in the first half, are no longer widening, and they will narrow sharply in early 1993."*

Everyone knows about the recession in Europe and Japan and about the decline in US manufacturing employment, but I think a sharp drop in profit margins in 1993 would be an unexpected shocker. At any rate, I don't hear anyone else talking about sharply sliding profits in '93.

THE PICTURE: Want to know how sneaky and deceptive this bear market is? John McGinley (*Technical Trends*, PO Box 792, Wilton, CT 06897) writes that *"31% of all stocks are lower than their 1987 lows, and most of the 1972 'nifty-fifty' are lower than their levels of that year! Merrill Lynch calculated that only 62% of stocks are over their 1987 highs."*

Yep, it's been confusing and deceptive, but my business is to try to make sense out of confusion, so here goes. We received a bear market signal under Dow Theory on October 5, a signal that tells us that the primary trend is down.

Despite that, my Primary Trend Index (PTI) has rallied to new highs. How can that be? Answer: It takes unusual selling pressure to push the two D-J Averages down below previous critical levels, and this is what occurred on October 5, the day of the bear signal. The market continued down until October 9, but at that point the market was severely oversold. That oversold situation is what triggered the rally following the October 9 lows. However, the rally in no way erased the validity of the bear signal. What the market is saying is that the tide is in the process of turning down, but the plug is not quite ready to be pulled.

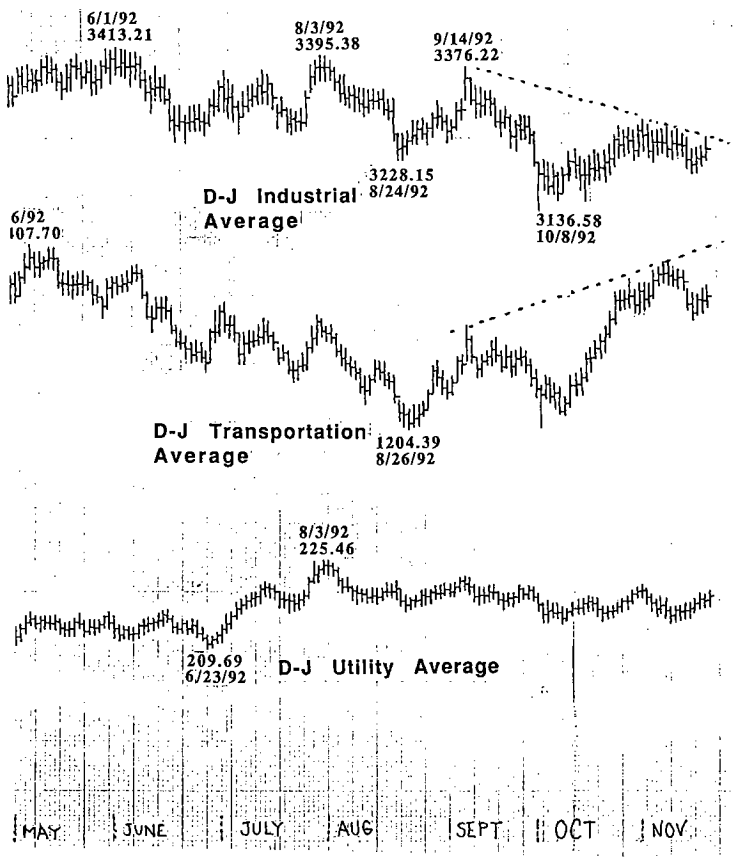
Consider this: the stock market (i.e., the broad composite averages) has gone nowhere since January, this despite all the actions of the Fed. And when I say Fed action I mean action which has been steadily pushing interest rates down, all the while flooding the banks with liquidity. Question -- why haven't low interest rates and the Fed reflation effort sent the stock market through the roof? My opinion: it's because the bull market topped out in February, and the subsequent bearish forces neutralized the reflationary action taken by the Fed.

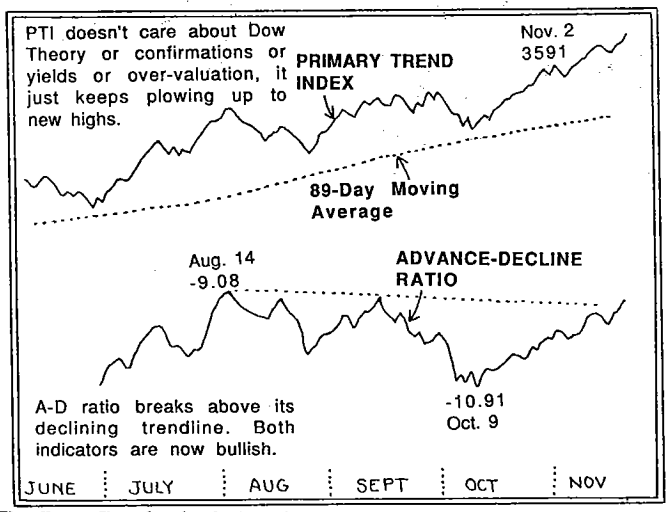
Nov. 13 DJIA 3233.03; PTI 3605; A-D Ratio -9.52
Nov. 20 DJIA 3227.36; PTI 3615; A-D Ratio -9.29
Dow Yield: 3.19%; Dow Price/Earnings: 43.2
Dow 200-day MA: 3290; Dow 30-day MA: 3203
Dow Times Book Value: 2.48; PTI 89-day MA: 3559
Percentage of Undervalued Blue-chips: 10%
Low Risk Buy Index: +125

And while the Fed was trying to reflate the economy, the public was cashing in its CDs and plowing tens of billions of dollars into the stock and bond markets (much of it into mutual funds). Again, why didn't this massive transfer of funds send the stock market on a spectacular rise to higher levels? Answer: the primary trend was working against the Fed and against the stockholders and against the new buyers. The bear was subtly getting his claws into the market.

THE AVERAGES: In the last Letter I drew attention to the flagrant non-confirmation in the D-J Averages. Specifically, I'm referring to the spurt in the Transportation Average well above its preceding peak (see the page 1 chart), while the Dow stubbornly refused to confirm. That non-confirmation remains in force as this Letter is written. And it's a negative.

200-DAY MOVING AVERAGE: I included a study of the 200-day MA of the Dow in the last Letter. The position of the Dow above or below its 200-day MA is always important to Dow Theorists. The reason is that the "big" stocks, the investment-grade stocks (as represented by the Dow stocks), are the ones that set the main trend of the market. A knowledge of the major trend of the market is crucial for investing, and the position of the Dow above or below its 200-day MA helps us to identify the main trend.





The Dow first broke below its 200-day MA on September 25. On that day the Dow closed at 3250.32. The Dow has held below its 200-day MA ever since. The 200-day MA now stands at 3290, and it is just rolling over and starting to decline. Based on my studies of the Dow and its MA, I would say that the longer the Dow remains below its 200-day MA, the more bearish the situation. The Dow has held below its 200-day MA for almost two months.

THE PTI: The record of my PTI has been pretty amazing. The PTI and its position above or below its own 89-day moving average has been the most accurate market indicator that I've ever dealt with.

But the PTI is no miracle indicator. In fact, here's what the PTI does not do. (1) The PTI does not deal with sentiment, it does not deal with opinion, it deals only with market action. (2) The PTI does not predict the extent or the duration of a move. (3) The PTI does not identify a move as being part of a bull or bear market. It simply tells you what is happening based on current action and statistics.

However, for identifying the current trend and telling you whether the current trend remains in force, I've never seen any index or market tool to equal the PTI.

TIGHT RANGE: There's a disposition for ALL markets and ALL items (stocks, bonds, commodities) to do nothing, to be inert. In fact, this is the essence of the option seller's game. The seller of options is betting that over a specified period of time nothing will happen and the option that he sold will expire worthless. On the other hand, the buyer of an option is betting that the item will move a certain distance within a specific period of time. Who will be the winner? Almost always the option seller. The statistic is that 85% of all options expire worthless. The option will not have rallied or declined strongly, as the option buyer expected it would.

If you study stock or commodity charts you will notice that most of the time the item is doing nothing, it is simply marking time. True, there will be sudden spurts up or down, but most of the time the item will simply be moving sideways, rallying a little or declining a bit.

Just in case you haven't realized it, this is about what's been happening to the markets here in 1992. Consider this-- last April 8 the S&P Composite dropped to a low of 394.50. From there the S&P rallied, hitting a high of 425.27. But last week the S&P was at 418, roughly 7 points below its high for the year. Thus, the S&P 500 has held in a narrow trading range of just over 7% ever since January.

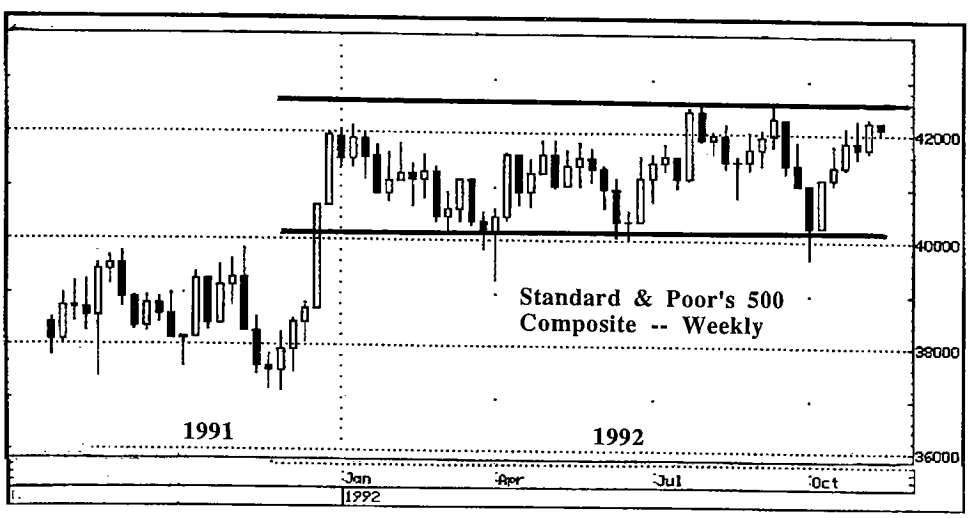
The NYSE Composite (which includes all NYSE stocks) recorded its low for the year on April 8 at 217.92. Following the low, the Composite rallied to a high of 233.73. Last week the NYSE Composite was at 228, roughly 5 points below the year's high. The range for the year, so far, on the broad NYSE Composite has been roughly 6.7%, not appreciably different from that of the S&P Composite.

On page 2 I have included a chart of the S&P Composite (weekly). This chart provides a dramatic picture of a market that has simply moved sideways, fluctuating within a tight band over the last 11 months.

By the way, this is a Japanese candlestick chart. The white bars denote rising weeks and the black bars denote declining weeks. The thin line tails or shadows denote the high and low of each week. I like candlestick charts, because they immediately highlight areas of accumulation or distribution.

Interestingly, since December, there have been 25 weeks in which the S&P closed higher and 20 weeks in which the S&P closed lower. So it's clear that 1992 has been a very indecisive year with the forces of accumulation and distribution very much in equilibrium. This is one of the longest such periods that I can ever remember. But there's that old adage, *"After the quiet comes the storm."*

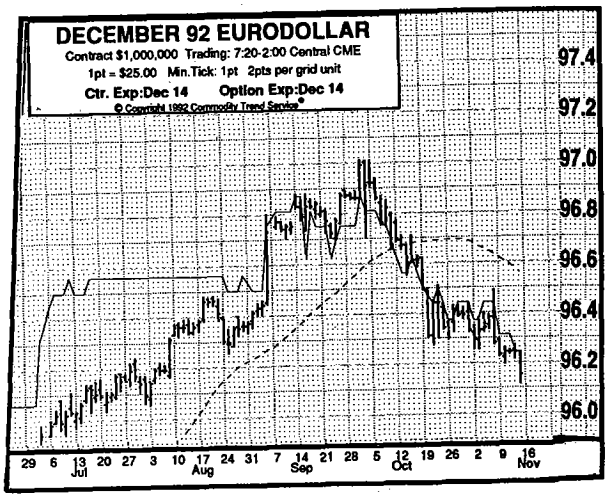
THE EUROS: Most people (professionals included) have little or no knowledge of the Eurodollar market. Eurodollars (the ones that are quoted and the ones the futures contracts are based on) are 91-day dollar CDs held outside the US. Whereas comparable 91-day T-bills are backed by the full faith and credit of the US government, Eurodollar CDs are backed only by the bank or the issuing company. However, the important fact is that the Eurodollar market is a totally free, unmanaged, unmanipulated market. It's a market the Fed has no control over. Thus, sophisticated professionals watch the Euros as the leading indicator of the direction of US interest rates.



As a matter of interest, the Eurodollar market is huge, estimated to be about $3 to $4 trillion. Trading in Euros dwarfs trading in T-bills. On a typical day there may be 350,000 Euro contracts traded (each contract worth one million dollars) as against maybe 8,000 T-bill contracts.

The Euros have topped out. They hit their highs in early October, and they have been dropping ever since. Consequently, Euro rates have risen a full 1% in yield from their lows (Euro rates are now slightly above 4%). Since Euros lead the way, this tells us that interest rates in the US have already hit bottom and are heading higher.

Rates in the US money market (bonds, notes, bills) have rather leisurely followed Euro rates up, but the sense I get is that the



US market hasn't quite tuned in to what the Euros are saying. For whatever reason, we've seen the lows for US rates. One caveat and it's a strong one -- if the US economy starts to slump, if the recession suddenly deepens, then I would expect the Fed to attack the rates again, dropping the discount rate and flooding the banks with even more reserves. Note: Since Sept. 9 adjusted reserves in the banking system have been rising at an incredible compounded annual rate of 27.6%. The Fed continues to flood the system with money.

But the fact is that rising short-term rates are poison to the stock market -- and short-term rates are rising.

CDs and the MARKET: All during the year the public has been pouring money into the stock market (much of it via mutual funds). Since February 1991, $407 billion in CDs have run off, and a large chunk of that money moved into stocks. This is money that was discouraged by the steady decline in CD rates; it's money that was hungry for higher yields and capital gains. My guess is that a major chunk of this CD money is owned by individuals, and I would also guess that a goodly portion of the stocks that were bought with CD money represent "money owned by the public," better known as "money in weak hands."

(Note: Here's part of an advertisement which appeared in last week's *San Diego Union*. One thing is clear -- the ad is not telling you to roll over your money into more CDs.) The implication is that you can do better elsewhere.

Your CDs are maturing--
Now what?

If you have money coming out of CDs, Money Market Funds, or Treasuries, you know rates are in a state of flux. What you may not know is what to do about it.

To find out more about what to do with cash, plan to attend Smith Barney's timely and informative seminar.

Wednesday, November 11th, 12:00 noon *(Luncheon served)*

As an aside, *Money* magazine states that over recent weeks as Bill Clinton headed for victory, Americans poured hundreds of millions of dollars into the shares of small companies and the mutual funds that hold small companies (this is according to data gathered for *Money* magazine's Small Investor Index).

So there's no question about it -- the American public has loaded up on stocks, and more recently with the stocks of "small companies."

This "combing the lists" for secondary winners is something I've seen many times before. Based on historical precedent, it's not a good sign. My guess is that investment grade stocks are being distributed while the public dives into the secondary stocks. Which is why the high capitalization stock averages have been moving sideways all year -- even while selected secondary stocks have spurted.

CDs and Stocks: Charles Biderman, who writes the very informative *"Market Trim Tabs"* (PO Box 2949, Santa Rosa, CA 95405) report, notes that during this whole public buying frenzy period the renewal rates vs. original rates on CDs have been dropping. In other words, those wanting to renew six-month CDs found that the renewal rates were well below their original rates (he terms this CD "sticker shock"). But, notes Biderman, rates are now only 70 points below the rates of six months ago. Moreover, rates have now risen 20 points from their recent lows.

Rates will only have to rise slightly higher and the negative CD renewal rates will disappear. At that point we will probably see the public selling stocks and going back to buying CDs.

Consequently, it's easy to see why the trend of short-term interest rates is particularly critical at this point (and I'm sure the Fed is well aware of this).

INVESTMENT POSITION: The slightly frazzled bear remains in the box. He's watching the public pour its money into mutual funds and into the secondary and smaller stocks. The bear is patient; he's biding his time.

Earlier I talked about the equilibrium in this market, the fact that for the past year there seems to have been an equal number of buyers and sellers, thus the sideways action in the major averages.

Aside from the smaller stocks and the speculative stocks, I always place most emphasis on the big investment-grade stocks, the kind that large investors tend to buy. Why? Because large investment interests set the trend of the market. They tend to be better judges of value, and they will be the first ones in at the bottom and the first ones out near the top.

Looking over the 30 Dow Industrials I don't see a great many good looking chart patterns. However, the following do look all right -- Allied Signal, Amer. Tel., Disney, Gen. Electric, Goodyear, McDonald's, MMM, JP Morgan, Procter & Gamble, Union Carbide.

Is there such a thing as a "Clinton stock?" Sure, and here's the Bill Clinton industry list courtesy of Ed Hyman of *International Strategy and Investment:* Engineering and construction, heavy trucks, electrical equipment, machinery, steel, semiconductors, publishing, pollution control, and hospital management -- by which I gather that Ed believes Clinton will get America building again, he'll get rid of all this darn pollution, he'll get you to a hospital if you break a leg, and he'll get America's illiterate millions reading again. Wot a guy! Listen, I hope it all works.

I've written before that in today's world with today's cross-currents the best position is a diversified one. I'd have most of my assets in cash (T -bills, muni money market funds, etc.), maybe 25% in hard foreign currencies, and around 5% to 10% in gold and gold related items.

The Hong Kong stocks I recommended have been bouncing around like rubber balls, swaying to the tune of the Hong Kong/China debates and altercations. Hong Kong's Hang Seng index has hit new record highs, then dived as the Chinese threaten and threaten again.

The Benham European Bond Fund has also been on the roller coaster, rallying up to 11.50, then sliding down to 10.45, then pushing up a bit. The key to this fund is the Deutschemark, which I think is bottoming now. I'm holding on to my shares of this fund.

As an aside, I have real doubts about the long-term future of the dollar. Pre-election promises and presidential performances are two different animals. Mr. Clinton promised a tax cut for the middle class and at the same time a reduction in the federal deficit. Frankly, I don't see how he can do it. Someday, instead of talking about slowing the rise in the deficit, some president is going to talk about actually reducing it. But by that time, the dollar may have lost another huge chunk of its purchasing power.

NOTES & QUOTES: I knew President Bush wasn't "tuned in," but I never realized how "out of it" he was and still is. According to the *NY Times* (Nov. 15) Bush is "deeply depressed" and "shocked at the election results." He blames a poorly run campaign and generally bad advice. Despite the polls, "Bush was described as having convinced himself that he would ultimately prevail." What was Bush thinking of? He lost the women's vote, he lost the gay vote (which is large), he lost the black and Latino vote, and he lost a lot of the liberal Republican vote and he even lost California. Bush's campaign, I thought, was ridiculous, all that concentration on Clinton's draft record and Clinton's "untrustworthiness." Americans were worried about jobs, not whether Clinton avoided the draft decades ago. Clinton had it right from the beginning, and it was posted on his wall -- "the economy, stupid."

A recent issue of *Time* magazine featured a picture of Mr. Clinton and headlined it, "Mandate For Change." Actually, from a popular vote standpoint, president-elect Clinton does not have a mandate for anything (but he'll probably get a lot of what he wants). Clinton captured 43% of the popular vote. That's actually 3% less than loser Dukakis got in 1988. Yet how bad was Bush's humiliation? He got 38% of the popular vote, which is all that George McGovern garnered in 1978.

From *US News & World Report* (Nov. 16): "Clinton faces one paramount obstacle in trying to spur the economy -- America's long-standing consumption habit. Nearly 50 cents of every dollar in federal spending is mailed off in a check to somebody, whether for Social Security benefits, for paying doctors to treat Medicare patients, or for subsidies to farmers or for giving poor people food stamps. In turn, government borrowing to finance this spending soaks up roughly two-thirds of all the private savings that would otherwise be available for capital investment. Thus Clinton and Congress must slash the deficit and curb consumption spending, especially for ballooning health programs . . . Although he has so far dodged talk of any pain, Clinton has no choice but to ask the public for sacrifices if he is serious about raising productivity." Russell comment: Good luck, Mr. Clinton.

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Somebody's getting a lot happier, as per this piece from *"W"* (Nov. 16), the magazine for the beautiful people. "Manhattan is rising from the dead. The city hasn't been this electric in years. Restaurants are packed, clubs are teeming and there are often five parties a night. Plays may be sold out for months ahead." Russell comment: I can tell you one thing that's happened -- Wall Street has been making lots of money. And when the financial guys and gals are making money, they spend it, and Manhattan gets giddy. For the first half of 1992 total compensation for Wall Streeters amounted to $12.2 billion with brokers earning $5 billion of that amount. The average salary for Wall Streeters this year should average an amazing $110,000. Gad, we could use a little of that action here in California. People aren't worrying about salaries or bonuses here, they're worried about pink slips.

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More California: This state is now facing its seventh consecutive year of drought, the worst sustained drought in 400 years (judging from tree rings). I only remember one rain in the last eight months, and that lasted for only part of one night. On top of that, California's budget deficit for 1993 is estimated at a minimum of $5 billion. Where's the money coming from? The higher they tax us (and they tax us high), the more real-earners leave the state.

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New York: Last week a Wells Fargo armored car hit a bump and dumped $311,000 in cash onto the Long Island Expressway. Passersby scrambled for the money. So far, Wells Fargo has collected $3,500. Said the Wells Fargo manager, "It was like they hadn't eaten in days. It was like throwing out a piece of meat to sharks." Russell comment: The bank got 1% back. That's not so bad.

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More Gotham: According to *New York* magazine, Donald Trump is back and maybe more exciting than ever. He may not have his former huge debts and big assets, but now he's got smaller debts and a percentage of his former assets. Trump's three casinos in Atlantic City are booming, Trump has a new girl friend (a Victoria's Secret model) and he sees himself as King of New York. The word is he's even writing a new book, something about coming back big from almost a billion in debt.

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Milestone: For the first time, financial institutions own more than 50% of US stocks. In fact, there are so many institutions involved with stocks that you might say that the institutions are the "odd-lot public" of the '90s (comparison: during the '60s the institutions owned 15% of all stocks).

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Sindlinger puts the current true inflation rate at 10.5%. He states that a good part of the difference between the Sindlinger Index and the government figures "is accounted for by the Sindlinger Index encompassing the costs of rising local taxes and insurance, particularly auto and health insurance. Those costs are not included in the CPI."

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Food: 75% of all restaurants in NYC either close or change hands within the first five years. Signs of the times: the average dinner price in NYC has dropped $1.35 over the last year. New Yorkers are eating out 3.1 times a week vs. 3.4 to 3.6 times a week during the '80s. NYC is still the priciest place to eat. Average price for a better-restaurant dinner in NYC is $32.48, well ahead of second place San Francisco at $27.31 per meal.

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It may be engineered like no other car, but it is also very darn expensive. Which may explain why Mercedes is in a worldwide slump. Of course, there's vicious competition from Infiniti, Lexus and BMW. Mercedes has the highest labor costs in the world (about 40% of Mercedes' $5.3 billion wage bill went for paid time off). In the meantime, the world auto slump is even hitting the Swedes where Volvo announces that it will lay off 4,500 workers.

When Ford bought Jaguar a few years ago for an unbelievable $2.5 billion I said that I thought it was one of the worst overpayments in corporate history. I don't think I was exaggerating. Jaguar's sales are now off 79.2% from 1991. Other horrors are Ferrari off 43.1%, Porsche off 23.7%, Alfa Romeo off 21.7%, Volvo off 8.7%. Winners are Lexus up 39.5% from last year, BMW up 14.6%, Infiniti up 7.4% and Acura up 4%.

About wages: Britain's auto wages are the lowest at just under $15 per hour. Japan runs $22 an hour, US about the same and German at almost $29 an hour (figures include fringe benefits).

GM has announced that it will raise another billion dollars, this time in preferred stock (estimated dividend will be around 8%). This is the eighth time since June '91 that GM has gone to the capital markets, and it will bring the amount raised from issuing new equity in the past year-and-a-half to a fantastic $7.9 billion. S&P threatens to drop the rating on GM debt. The huge auto maker is still downsizing and plans to cut at least 74,000 jobs and close 21 plants by 1995. Russell opinion: In recent months, GM's N. American operations have burned up cash almost as fast as the company could raise it. GM is going to have to do a lot of things right and it is going to need a lot of luck if it is to survive in anything like its current form.

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Gambling: We just got back from Vegas. I've always wanted to see a heavyweight championship fight in Vegas and we did it. But it wasn't easy. We were told the fight would be at the Mirage. When we got there we were told that the fight was being transferred to the Thomas & Mack stadium. I asked, "How do we get there? Do you

provide any transportation?" Answer, "Nope, find a taxi." We spent 45 minutes looking for a taxi, finally got one and at 5:30 headed for the stadium five miles away. "With 20,000 people looking for taxis after the fight," I asked Faye, "I wonder how we're supposed to get back?"

At any rate, we saw the fight, which was truly a great one. Dozens of celebs there, but the crowd's biggest shouts were for George Foreman and Magic Johnson. The fight over, we walked out and lo, Caesar's Palace had about 25 big buses waiting to take people back to their hotels. Of course they landed everyone in front of the casino at Caesar's, but that was OK. Caesar's was probably crushed when they found out that Faye and I don't gamble, but believe me, we were grateful for the transportation. Thanks Caesar's.

A week before I happened to talk to a lady who had worked in the Vegas casinos for 20 years. I asked her, "I've always wondered, what happens to the people who come to Vegas and are wiped out gambling -- how do they get home? I've heard the casinos give them bus fare home. Is that true?" The lady laughed, "If you have no money they don't even know you. You can hitch hike back to LA or Cleveland as far as the casinos care. When you're broke in Vegas, brother, you're on your own."

According to Rock Newman, Riddick Bowe's manager, the Chinese government (can you believe it?) has offered to pay $20 million (a site fee) for a Bowe-George Foreman fight in Beijing. Said Newman, "It would be the biggest grossing fight of all time." The Nov. 15 *LA* magazine has a lead piece on huge rock-and-roll concerts in China. What's happening there? I can tell you. They're making money (at least South China is, and money talks, even in dictatorships).

As late as the '60s the mob controlled gambling in Las Vegas. But the big money companies such as Hilton Hotels, Holiday Inns, Circus Circus bought the mob out. And with large corporations now in control, gambling is expanding far beyond the wildest dreams of the mob. It's gambling from New Orleans to Chicago to California. In fact, every state in the Union but Utah and Hawaii has some form of gambling. Here in California it's poker, which is considered a "game of skill." And it's gambling at the Indian reservations.

My son-in-law went to Vegas last week to enter the "World's Championship of Poker." It used to cost $10,000 to enter this game, but this year they did two things. They reduced the entrance fee to $5,000, and they set up a $200 alternative. For $200 you play against nine other players. If you beat the other nine, you can join the big boys and start against them with $5,000 in chips. At least in this kind of gambling, your losses are limited to the entrance fee, $200 or $5,000.

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The last two holdouts for dictatorship, North Korea and Cuba, are in economic trouble and looking for Free World investors. The talk is that Castro won't last another three years and that N. Korea will ultimately unite with S. Korea. When your neighbors are living well and making money, the word gets out, and that's what's been happening in N. Korea and Cuba. I've said this before, in a battle of economics vs. politics -- economics will always win. Maybe the Soviets are the greatest proof of that.

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Diamond prices are a bit wobbly, although large (over 8 carats) gem quality diamonds are still a costly rarity. But there's a new source for diamonds, the Lac de Gras area of Canada's Northwest Territories. The word is that it may rival Botswana, the world's biggest producer of gem diamonds. Already 16,000 square miles of the Territory have been staked in what has been termed the biggest rush for land ever seen in North America. The Point Lake Pipe is said to be "giving world-class results in diamonds estimated at a value of $2 billion for this one pipe alone."

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This is from my friend, Chris Wood, the *Economist's* finance editor for Japan (Chris is stationed in Tokyo): "Japan faces a financial crisis as severe as the US S&L debacle. There is nearly $500 billion of problem debt in the banking system. The money supply is shrinking, and bank lending is barely growing. Land prices have plunged, and the stock market remains more than 50% off its all-time high. Companies face their third straight year of declining profits for the first time since 1945, with the car and electronics export industries bearing most of the pain. It may be only months before major companies start a large-scale dismissal of employees; if they don't, profits will be down for a fourth year in a row. Sensing all this, consumers have turned cautious." Russell comment: The Japanese government a week ago stated that non-performing loans on the books of Japan's leading banks stand at $100 billion. Chris may be an optimist.

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The New York auctions are now in progress, and they provide an insight into what the big money will pay for art. So far, the mood is restrained, if not disappointing. In most cases, prices fell. Examples: A Renoir painting that sold in London to a Japanese investor for $2 million in 1988 went for $797,000. A Klimpt that was sold in 1989 for $4.6 million went for $2 million. Said a world renowned dealer, "It was a disappointment. We had expected a better sale because there was so much enthusiasm during the viewing. "

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Government Stupidity Dept: In the past budget year the Pentagon has cut 178,024 sailors, soldiers, airmen and Marines from active duty. That's the largest single-year cut in twenty years. Current plans are for 160,000 more service people to be cut. Russell question: In view of the above, why the devil is the government spending our tax money on new enlistment ads. The Marines don't need "a few good men." The fact is they need fewer good men.

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A subscriber asked, "Russell, what would you do if you were Clinton?" I immediately answered, "I'd put all my strength and prestige into getting rid of the current tax system. It's an outrage, a pure political boondoggle. I'd opt for a 20% flat tax -- no corporate tax, no capital gains tax. Then I'd go through the government like a giant meat (pork) slicer, cutting out whole departments and cutting existing departments to the bone. I'd change the crazy Social Security system to a funded private system, and I'd end the whole 'off-budget' scam, a mechanism that hides America's true deficits."

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Russell Grouse: I grew up with jazz and swing, with Benny Goodman and Frankie, with Duke Ellington and Count Basie. Later I loved early rock-and-roll, I liked the Detroit sound, I like country and western, I like Gershwin and I like Beethoven. My kids like MTV and they like rap. To my mind, the music I hear on MTV is the absolute worst, the most unmusical, the most annoying that I can ever remember. And I agree with current Trumpet great, Wynton Marsalis, when he says, "Contemporary pop songs aren't even melodies, man. It's like something you would envision cave men doing. You can go back to the earliest forms of American music, and it doesn't sound that elemental. I've been saying this for 10 years and getting attacked for it, but that's what the truth is."

BEAR MARKET VALUATIONS: I'm often asked where stocks could go in a big bear market. My friend Gerry Weiss publishes the excellent *Investment Quality Trends* here in La Jolla (7440 Girard Ave., La Jolla, CA 92037). Last week she put out a list of blue-chip stocks that are particularly vulnerable. The list shows the recent price and yield, and then it shows where the stock could go if the bear market takes it from the current overvaluation to the opposite extreme -- undervaluation. I thought the list was an eye-opener. It's worth studying carefully. (Note: Each stock has its own historical yield band, and for undervaluation the high-yield end of the band is used.)

PERILOUS BLUE CHIP HOLDINGS

Stocks with downside risks of 65% or more from current price levels.

STOCK	RECENT PRICE/YIELD		DOWNSIDE RISK POINTS/PERCENT		UNDERVALUED PRICE/YIELD	
AFLAC	30	1.5%	24	80%	6	8.0%
ALBERTO CULVER	25	1.0%	22	88%	3	7.0%
ALBERTSONS	46	1.4%	33	72%	13	5.0%
AVEMCO	24	1.7%	17	71%	7	6.0%
BANDAG	59	1.0%	44	75%	21	6.0%

STOCK	RECENT PRICE/YIELD		DOWNSIDE RISK POINTS/PERCENT		UNDERVALUED PRICE/YIELD	
BAUSCH & LOMB	54	1.5%	35	65%	19	4.3%
BEMIS COMPANY	23	2.0%	16	70%	7	7.0%
BLOCK DRUG	47	1.9%	32	68%	15	6.0%
CAMPBELL SOUP	42	1.9%	31	74%	11	7.0%
CAPITAL HOLDING	62	2.1%	41	66%	21	6.3%
CARTER WALLACE	28	1.2%	23	82%	5	6.6%
CENTEL CORP	63	2.7%	22	67%	11	8.5%
CHUBB CORP	86	1.9%	61	71%	25	6.5%
COCA COLA	41	1.4%	30	73%	11	5.0%
CONAGRA	30	2.1%	21	70%	9	6.7%
COOPER TIRE-RUBBER	32	0.6%	30	94%	2	8.0%
CROMPTON & KNOWLES	19	1.7%	14	74%	5	6.7%
DISNEY, WALT	39	0.5%	31	79%	8	2.5%
DREYFUS CORP	38	1.8%	28	74%	10	6.5%
FEDERAL SIGNAL	20	2.1%	13	65%	7	6.0%
GAP INCORPORATED	31	1.0%	20	65%	11	3.0%
GERBER PRODUCTS	35	2.3%	24	69%	11	7.5%
GILLETTE	59	1.2%	49	83%	10	7.0%
GRAINGER, W.W.	57	1.2%	38	67%	19	3.5%
GREAT LAKES CHEM	70	0.5%	51	73%	19	1.7%
HANNAFORD BROS	20	1.5%	15	75%	5	6.6%
HERSHEY FOODS	46	2.3%	30	65%	16	6.8%
HILLENBRAND	40	0.9%	33	83%	7	5.0%
HORMEL COMPANY	20	1.8%	14	70%	6	6.2%
HOUGHTON MIFFLIN	36	2.2%	25	69%	11	7.3%
ILLINOIS TOOL WKS	66	1.5%	45	68%	21	4.5%
INTERPUBLIC GROUP	33	1.4%	25	76%	8	6.0%
KELLOGG	73	1.8%	52	71%	21	6.0%
MANOR CARE	21	0.4%	18	86%	3	2.8%
MARTIN MARIETTA	57	2.9%	37	65%	20	8.5%
MAY DEPT STORES	69	2.4%	48	70%	21	8.0%
MEDTRONIC	96	0.6%	77	80%	19	2.9%
MOTOROLA	97	0.8%	72	74%	25	3.0%
NEWELL COMPANY	39	1.5%	31	79%	8	7.7%
NORWEST CORP	41	2.8%	27	66%	14	8.2%
NUCOR CORP	59	0.5%	39	66%	20	1.4%
PARAMOUNT COMMUN	43	1.9%	30	70%	13	6.0%
PEPSICO	39	1.3%	29	74%	10	5.0%
PREMIER INDUS	36	1.3%	24	67%	12	4.0%
RUBBERMAID	32	1.2%	23	72%	9	4.5%
SARA LEE CORP	58	1.7%	44	76%	14	7.0%
SCOTT PAPER	37	2.2%	25	68%	12	6.5%
SHAW INDUSTRIES	26	1.2%	20	77%	6	5.0%
SHERWIN WILLIAMS	29	1.5%	20	69%	9	5.0%
SMUCKER, J.M.	28	1.5%	21	75%	7	6.4%
STRIDE RITE	19	1.6%	15	79%	4	8.0%
TAMBRANDS	65	2.3%	43	66%	22	7.0%
TOOTSIE ROLL	80	0.4%	74	93%	6	5.0%
TORCHMARK	54	2.0%	38	70%	16	6.7%
TYCO LABS	40	0.9%	34	85%	6	6.5%
UJB FINANCIAL	18	3.3%	12	67%	6	9.9%
UNIVERSAL FOODS	32	2.8%	22	69%	10	9.0%
VF CORP	51	2.1%	37	73%	14	8.0%
VALSPAR CORP	32	1.1%	26	81%	6	6.0%
WAL-MART STORES	62	0.3%	51	82%	11	2.0%
WALGREEN	40	1.5%	31	78%	9	6.7%
WELLS FARGO	69	2.9%	45	65%	24	8.9%
WINN-DIXIE STORES	67	2.0%	45	67%	22	6.0%
WRIGLEY, WM	33	1.2%	22	67%	11	3.6%

GOLD: I obviously can't prove it, but I do get the feeling that every time gold "wants to" rally, someone, somewhere, moves in to knock it down. Could this be the work (clandestine) of the Fed? I don't know. The rumor is that various central banks are selling gold to raise cash -- I don't know about this either. But if you want to raise cash, you don't have to sell your gold assets, you can simply borrow against it.

Corporate profits are being squeezed in many areas, and one of the big problems is that costs have risen, but there is terrific resistance to price boosts. Furthermore, competition is intense (check the computer and software industry for an example of vicious competition). Of course, there's one way to help out, and that way is called inflation or lifting prices. There's tremendous incentive in the US to do this, but consumer resistance has prevented it. Therefore, the squeeze continues, and corporations have sought to increase profits by cutting workers, a process that is still going on.

However, despite all predictions, gold is hanging on, and all the gold that is being sold by the central banks is being bought by someone and put away.

LATE NOTES & THOUGHTS: I hate to belabor the California case, but California is the nation's most populous state, and what happens here has to affect the nation. This headline from the *LA Times* came out on November 20, and I just look at it and shake my head. The state is in an unbelievable bind, and I can't figure how it can continue to handle its massive overspending.

State warned of $7.5 billion deficit in '94

Gap could even top $9 billion, analyst says; budget fight looms

By DANA WILKIE
Staff Writer

A state analyst said yesterday that California's budget may be $7.5 billion to $9.3 billion out of

said Hill, whose office provides an independent analysis of state finances

Wilson points to recession

Every agency in the state seems to be running at a deficit, and the situation appears to be deteriorating rather than getting better. Stay tuned.

I'm sitting here watching the stock market tape (of course it isn't a tape any more, I think I'm showing my age), and it's really amazing. The market keeps pushing and pushing, despite the collapse in IBM, despite the shocking drop of Westinghouse below 10, despite GM flirting with 30, and most extraordinarily -- despite currently rising short-term rates.

Remember, all during the recession the market climbed as it responded to drop after drop in the short rates. The word was that "people have nowhere to go with their T-bill and CD money except the stock market." But now with short rates rising, it will be interesting to see if the stock market can continue to ignore this new phenomenon.

The feeling I get is that the public just can't wait to get into the market, and if they're not buying individual stocks they're sending their money to a mutual fund -- whereupon the fund turns around and buys stocks.

Overvaluation, so far, has meant nothing to this market -- but it will. An understanding and appreciation of values is the single most important consideration in buying or selling stocks. Investment-grade stocks have been overvalued for over a year now, and I would say that this flagrant overvaluation is the single most important consideration in the stock market today.

My **PTI** measures eight critical action-of-the-market indicators. Actually, what the PTI tells me on a daily basis is whether the "action" of the market is good or bad. There's no question about it, the ACTION of the market continues good. I literally can't get a bad day out of the PTI.

When this market finally turns undeniably bearish, the opposite will be true -- I won't be able to get a good day's reading out of the PTI. That just hasn't happened yet.

Markets that go to extremes, markets that appear to be doing the impossible, are always fascinating. Old timers shake their heads in disbelief, and neophyte analysts explain (usually in magazine columns or newspaper interviews) why "this time it's different," and why the current trend will continue into the distant future.

It's all part of the great Wall Street game. I've been watching the game for 45 years, and it still has me puzzled probably 50% of the time. I guess the truest adage in the market is this -- "The market always does what it's supposed to -- but NEVER WHEN."

FINAL NOTES: On Friday, Nov. 20, both the NYSE Composite and the S&P 500 closed at new record highs. For the third time this year the Dow refused to confirm. Don't think I've ever seen this kind of action before. Obviously a lot of speculation with the big-cap Dow stocks not wanting to go to new highs. Meanwhile, short rates continue to creep higher. Stocks dangerously overvalued with Barron's highest grade bonds now yielding 2.57 times the 3.19 yield on the Dow.

NEXT MAILING: Dec. 9, 1992